

FACT SHEET FOR PARTNERS

Katrina Emergency Tax Relief Act of 2005



Key Provisions

- Suspends personal casualty loss from AGI and floor restrictions
- Waives penalties for early withdrawal of IRA and retirement accounts
- Expands qualified plan loan limits
- Raises the standard mileage rates for volunteers
- Allows use of 2004 income data to compute 2005 EITC
- Excludes discharge of indebtedness income
- Extends replacement period for gain non-recognition
- Suspends limits on charitable deductions
- Expands the food and book inventories donation deduction
- Offers Work Opportunity and New Employee Retention Credits

Hurricane Katrina wreaked havoc on the Gulf Coast, prompting a strong congressional response and a call to action from various federal agencies, including the Internal Revenue Service. This fact sheet summarizes the portions of the Katrina Emergency Tax Relief Act of 2005 that impact individual taxpayers.

Before we begin the summary, we want to share with you immediate steps we are taking to address the impact this disaster has made to our Volunteer Return Preparation Program (VRPP).

- We are holding conversations with local and national partners to determine capabilities for volunteer assistance in 2006 and to identify potential resource needs.
- We are preparing a training supplement covering the individual tax law issues that will be covered in the VRPP. This training will be delivered by December.
- Tax law surrounding casualty loss is very complex. Therefore, we have made the decision we will not be handling tax returns with casualty loss situations at volunteer sites. We are exploring options so that volunteers can properly refer taxpayers with casualty losses to alternative forms of assistance.
- We recognize that due to extensive flooding and damage, many taxpayers may have lost necessary filing documentation and paperwork. A national IRS team has been convened to address these very issues. We will communicate decisions as soon as they are made.

Important Facts to Know About the New Law

- The Katrina Emergency Tax Relief Act of 2005 postpones the deadlines for affected taxpayers to file returns, pay taxes and perform other time-sensitive acts until February 28, 2006.
- Tax relief is automatic for those in areas designated by FEMA as individual assistance areas. Extensions are automatic. Taxpayers do not need to do anything to get the extensions and other available relief.

- Taxpayers need to identify themselves as hurricane victims by writing **Hurricane Katrina** in red ink at the top of their tax forms or any other documents filed with the IRS.
- IRS.gov contains a wealth of Katrina-related information. If taxpayers need to contact the IRS or have other hurricane-related tax questions, they can also call the special IRS disaster hotline at: **1-866-562-5227**.

Help for Individuals

- **Relief from early withdrawals from retirement plans.** Victims may withdraw up to \$100,000 from an IRA, 401(k) plan or similar savings plan without penalty for distributions made on or after August 25, 2005, and before January 1, 2007. In addition, they would not be taxed on withdrawals that are repaid within three years and would be permitted to pay income tax on other withdrawals over a three-year period. Finally, Katrina victims who withdrew funds from an IRA after February 28, 2005, and before August 29, 2005 for a first-time home purchase but who could not complete that purchase, may put the funds back in their IRAs without penalty, if done so by February 28, 2006.
- **Temporary Suspension of Limitations on Charitable Contributions.** In the case of an individual, the deduction for qualified contributions is allowed up to the amount by which the taxpayer's contribution base exceeds the deduction for other contributions.
- **Additional exemption for housing individuals displaced by Katrina.** Individuals who use their principle residence to provide free housing to evacuees for at least 60 consecutive days may claim a special \$500 deduction from taxable income for each evacuee. The deduction may be claimed in 2005 and 2006 for eligible individuals but is capped at \$2,000 total for both tax years. The shelter must be in the taxpayer's principle residence and the evacuee's principle residence must have been in the Hurricane Katrina disaster area as of August 28, 2005.
- **Increase in the standard mileage rate for charitable use of passenger autos.** The optional standard mileage rates for miles driven between September 1 and December 31, 2005 has increased to 48.5 cents for all business driving and 22 cents per mile for moving or medical reasons. The law also increased the mileage rate for determining the tax deduction for the charitable use of an automobile to provide Hurricane Katrina disaster relief to 70 percent of the standard mileage rate in effect for business usage. The mileage rate for taxpayers providing service to charitable organizations remains at 14 cents per mile.
- **Charitable mileage reimbursements.** The reimbursement received by a volunteer from an organization described in Code Section 170(c) is excluded from his or her gross income up to the amount that equals the full standard business mileage rate. This exclusion provision applies during the period beginning August 25, 2005 and ending on December 31, 2006.

- **Special rule for determining earned income.** Katrina victims may use their 2004 income to calculate the additional child tax and the earned income tax credits for a tax year that included August 25, 2005. To be eligible, taxpayers must have lived in (1) the core disaster area or (2) the Hurricane Katrina disaster area and been displaced from his or her home by reason of Hurricane Katrina, as of August 25, 2005. The earned income for 2005 must be less than 2004 earned income.
- **Casualty losses.** Casualty losses in the Hurricane Katrina disaster area on or after August 25, 2005 are not subject to the 10 percent of taxpayer's adjusted gross income and the \$100 floor restrictions.
- **Extended tax deadlines.** Qualifying taxpayers have until February 28, 2006 to file any returns and pay taxes for any period that had not expired before August 25, 2005.
- **Cancellation of indebtedness.** Excludes certain discharges of indebtedness for victims located in the core disaster area or in the Hurricane Katrina disaster area who suffered economic loss. The debt provision applies to discharges made on or after August 25, 2005 and before January 1, 2007.

Help for Business and Corporations

- **Work Opportunity Tax Credit.** Encourages employers to hire individuals impacted by Hurricane Katrina. The credit generally equals 40 percent of the first \$6,000 of wages paid to each targeted group member during the first year of employment.
- **Employee Retention Credit.** Encourages small businesses to keep employees on their payroll. The credit is 40 percent of the first \$6,000 in wages paid to each eligible employee after August 28, 2005 by employers located in the core disaster area.
- **Corporate donations.** Waives the 10 percent limitation for Hurricane Katrina cash donations made by corporate donors to a qualified charitable organization between August 28 and December 31, 2005.
- **Food and book inventory donations.** Enhances the deductions for qualified organizations donating food and books.

***This summary is provided for informational purposes only.
It should not be used as a source for tax administration.***